Inland Natural Gas Co. Ltd. 1977 Annual Report

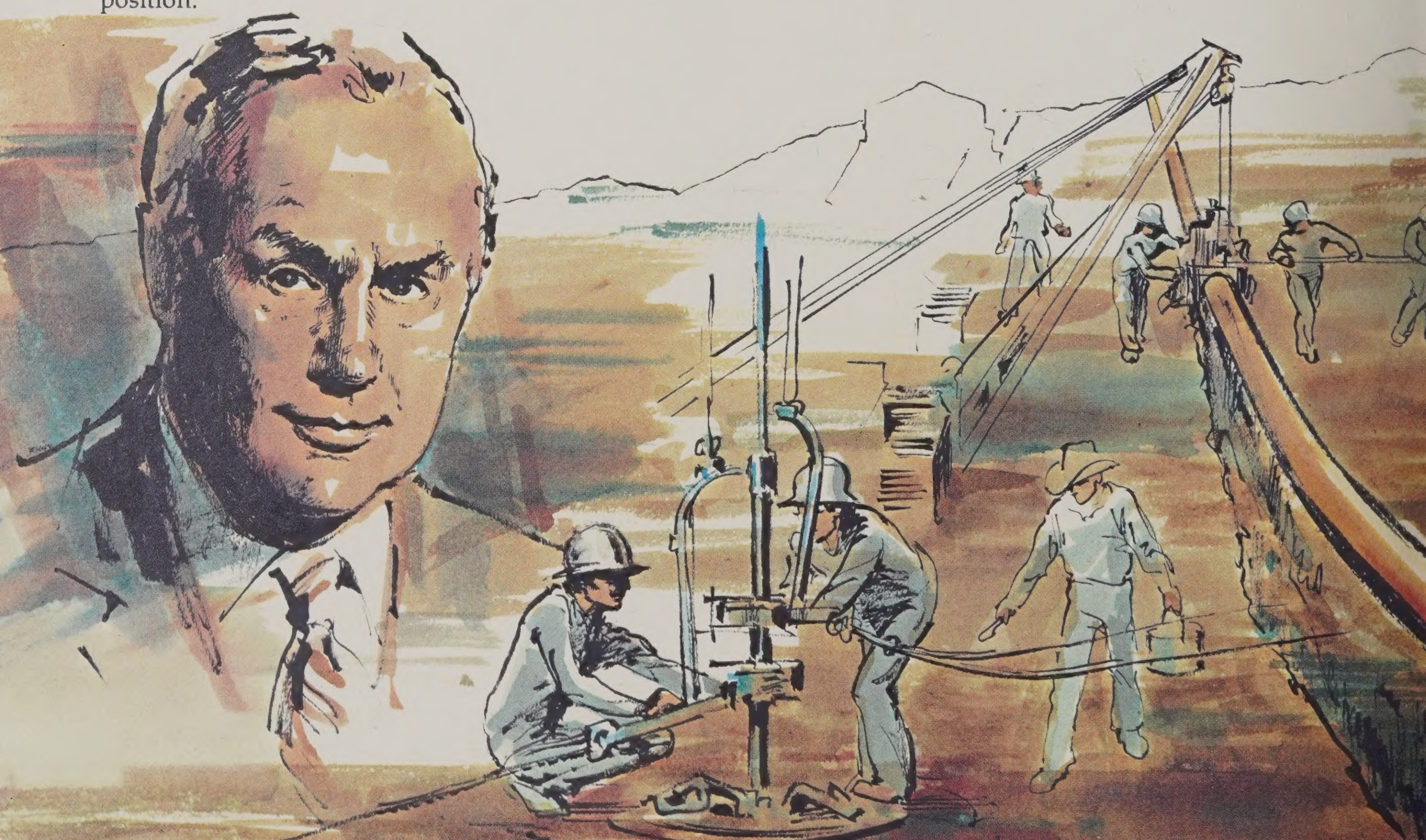
25 Years of Progress

Twenty-five years ago in June 1952, Inland Natural Gas Co. Ltd. was registered as a British Columbia Company. It was an event that would later have a major impact on the economy of British Columbia's interior. Prominent among the Company's founders were John A. McMahon and Norman R. Whittall, both well known Vancouver businessmen. Mr. Whittall was the Company's first President and in 1955 was elected Chairman of the Board. He remained active in the affairs of Inland until his retirement from the Board in 1973. Mr. McMahon played a particularly important role in the Company's history as President and later as Chairman of the Board and Chief Executive Officer. Following his death in November, 1972, the Board of Directors recorded a eulogy which read in part:

> "His personal knowledge of the problems of the Province of British Columbia, his imagination and his personal faith in the growth of the Province was a major asset in guiding the Company to its present position."

Inland's first major activity was the acquisition of several petroleum and natural gas related subsidiary companies, St. John Gas & Oil Ltd. (N.P.L.), Peace River Transmission Company Limited, Canadian Northern Oil & Gas Co. Ltd. (N.P.L.) and Grande Prairie Transmission Co. Ltd. Inland has since disposed of its interests in Canadian Northern Oil and Gas Co. Ltd.

By 1957 Inland had arranged the necessary financing, long-term natural gas contracts, pipeline right-of-way, certificates and franchise agreements to permit commencement of distribution facilities in twenty-seven B.C. interior communities located in a service area which extended almost 1,000 miles from Chetwynd in the north to Nelson in the southeast, with a population estimated at 225,000. The Company served northern communities with laterals off the Westcoast Transmission Company Limited line and built its own transmission line to serve the Okanagan and Kootenay areas of the province.



Construction of Inland's 360 miles of transmission lines began in February, 1957 and traversed some extremely rugged terrain including the Cascade Mountain Range where the line climbed to its highest point at 5,280 feet. Along the route were three major river crossings, two aerial bridges over the Columbia and Kootenay Rivers and a submerged crossing of the Quesnel River. The new system was put into service in September of 1957 to supply initially 6,000 customers. Since that date, Inland through aggressive sales and expansion policies has taken advantage of the rapid industrial, commercial and residential growth in its service area.

By 1971, Inland's customer count had reached 42,000 and a decision was made to build a 102-mile 12″ transmission line from Kingsvale to Oliver to reinforce supply. The route lay essentially through the Similkameen Valley. This new transmission facility permitted Inland to extend service to several additional communities. Also part of the reinforcement plan was the construction of two new 1,100 H.P. compressor stations at Savona and Kingsvale. These units were placed in service the following year.

In 1975 construction of the East Kootenay Link was completed. It was the largest single addition to the Company's transmission facilities since construction of the original system in 1957. Permission to build the 103.4-mile 12″ pipeline connecting the Alberta Natural Gas transmission line near the British Columbia-Idaho border at Yahk to the south end of Inland's system near Trail had been sought for some time. It allowed Inland to buy quantities of Alberta natural gas in peak winter months and return equivalent British Columbia gas to the Alberta system during the summer, increasing the overall efficiency of Inland's system and at the same time providing an alternate source of supply adding to security of service over the entire southern distribution area.

The Company now serves over 70,000 customers in 49 communities in a service area that presently has an estimated population of close to 500,000 which is projected to increase to approximately 1,000,000 by the year 2000.

Highlights

R. L. Cliff, Chairman of the Board

EARNINGS AND DIVIDENDS	1977	1976
Net Income	**$ 5,497,041**	$ 4,805,917
Common Shares Outstanding	**2,822,122**	2,822,122
Earnings per Common Share	**$ 1.44**	$ 1.56
Dividends per Common Share	**$ .80**	$ .80
Dividends per Preference Share	**$ 1.00**	$ 1.00
Dividends per Second Preference Share	**$ 2.61**	$ —

REVENUES AND CUSTOMERS		
Total Revenue	**$ 53,093,875**	$38,296,766
Total Gas Sales Revenue	**$51,621,709**	$37,471,711
Total Gas Sales Volume (MMcf)	**43,173**	37,726
Number of Customers	**71,451**	67,434
Degree Days (base 18°C)	**3,763**	4,018

PROPERTY, PLANT AND EQUIPMENT		
Additions for the Year	**$ 8,257,079**	$ 14,392,029
Total Investment	**$112,739,727**	$105,377,899

ANNUAL MEETING

11:00 a.m. (Vancouver time) October 27, 1977,
Four Seasons Hotel, Vancouver, B.C.

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To Our Shareholders

Earnings per share for the year under review amounted to $1.44, down 12¢ from the previous year. Revenues were up 39% over the previous year. The major reason for the increase in revenue is a result of the "tracking" of wholesale price increases and our own interim rate increase that became effective January 2, 1976. The increases in revenue and expenses are explained in detail in the body of the report. The decline in earnings per share is primarily the result of the effects of inflation on the Company's costs of doing business and increased preference dividends necessitated by the issue of additional preference shares in June, 1976. The recent decision of the British Columbia Energy Commission regarding the Company's retail rates to its customers will not, in the opinion of the Company, fully arrest this decline in earnings and the Company will apply for an additional rate increase as promptly as events will permit.

Last year we reported a significant increase in drilling activity within the province. It is gratifying to report that the increased activity has continued for the second consecutive year with the expectation that 90 to 100 wells will be connected this calendar year. This welcomed improvement will obviously result in an improved future gas supply picture for the province.

Although our major supplier, Westcoast Transmission Company Limited, has not been able to supply the full export volume allowable under its licence, Westcoast has met its contractual obligations to your Company. Our projections indicate that we will reach the maximum contractual daily volume allowed under the existing contract with Westcoast by November 1, 1979. During the past few years your Company has been unsuccessful in negotiating an increase in this contractual volume with Westcoast. On April 4, 1977, the British Columbia Government announced their support of certain arrangements between Westcoast and Pan-Alberta Gas for the movement of natural gas from Alberta to Westcoast's U.S. customer, Northwest Pipeline Corporation, to assist in meeting the British Columbia shortfall on the Westcoast export licence. In the same announcement, the Government stated that this arrangement will lift the contract restrictions on the sale of gas from Westcoast to the British Columbia utilities. Since that announcement we have received a letter from Westcoast indicating their willingness to discuss contracting for volumes of gas in excess of our current limits. Contract talks are currently underway.

In June 1977, the British Columbia Energy Commission held a hearing concerning the natural gas industry in the province. Your Company presented to this hearing a 25-year market forecast prepared independently for us by Canadian Resourcecon Limited. This forecast predicts that the area serviced by Inland will continue to experience growth at a rate above the Provincial average. It further predicts that natural gas sales volume to all classes of customers will increase at a compounded annual rate of 3.2% over the forecast period. The market penetration of natural gas in the residential section is expected to grow from its current level of approximately 47% to 65% by the year 2001.

Since 1955 Inland has obtained franchise agreements or equivalent rights with almost all of the incorporated municipalities in which it distributes natural gas. These agreements or rights are for a term of 20 or 21 years and are basically similar in form. The agreements contain a provision to the effect that at the end of their term the municipality may purchase the Company's distribution system within the municipality at a price which shall be the fair value of business and undertakings as a going concern. These agreements are now coming due for renegotiation and none of the communities serviced have indicated their intention to exercise the purchase option. Ten franchise agreements have received Order-in-Council approval for renewal and while negotiations have been extensive, the Company fully expects to renew all agreements. As discussed at greater length in the body of the report, the British Columbia Energy Commission has announced that it will hold a hearing in the Fall of 1977 with respect to franchise fees.

The decline in earnings this year will require the full energy and imagination of your employees and your Board to achieve the financial results required and expected in the years ahead. We meet this challenge with optimism and an unequivocable confidence in the Company and its future. In achieving our goal we are mindful of an improving natural gas supply picture, together with a growing market area and a product which we can offer on a very competitive basis.

Vancouver, B.C.
September 28, 1977

R. Landel [signature]
Chairman of the Board

President and Chief Operating Officer

Directors' Report

REVENUE

Consolidated gross revenue for the year under review amounted to $53,093,875 compared to $38,296,766 last year. Revenue from gas sales, most of which is derived from the parent company, rose to $51,621,709 compared to $37,471,711 a year ago. A large part of this gain can be attributed to substantial increases in the retail price of natural gas, much of which resulted from wholesale price increases which flowed through to Inland's customers with the consent of the B.C. Energy Commission, and did not improve the net income of the Company. The Company applied for interim rate relief in the fall of 1975 and was granted an interim rate increase of 7¢ per Mcf to all customer classifications effective January 2, 1976. This interim rate increase, which was only in effect for 6 months of the previous fiscal year, was still in effect at June 30, 1977 and, therefore, gave rise to substantial additional revenue in the year under review. Inland's sales volume for the year was 40,200,000 Mcf compared to 34,600,000 Mcf in the previous year. In spite of the addition of just over 4,000 residential and commercial customers during the year, gas sales to these customer categories were slightly lower than the previous year due to weather that was 8% warmer than normal. Industrial volumes, however, rose 27% to 26,532,000 Mcf. Part of this increase reflects the loss of sales in fiscal 1976 due to prolonged labour strikes in the pulp and paper industry. Also included in industrial sales for the year were certain spot sales last fall to Columbia Natural Gas Limited which totalled approximately 800,000 Mcf.

Transportation revenue increased from $296,700 to $825,950 during the year due to a temporary arrangement whereby Inland delivered quantities of gas from Alberta into its service area for consumption by Inland customers through its pipeline connection at Yahk. This allowed Westcoast Transmission Company Limited to reduce deliveries to Inland and increase deliveries by equal quantities of such gas to the U.S. border to help alleviate a shortfall in supply to its U.S. customer. Westcoast paid Inland a transportation fee for this service.

Since the commencement of operations in 1957 Inland has been receiving, under its contract with Westcoast, a monthly transportation allowance which for many years has amounted to $24,725 per month. This contractual arrangement will expire on October 31, 1977.

Other operating revenue increased as a result of profit from the sale of certain properties of the Company and of its subsidiary, Inland Development Co. Ltd.

EXPENSES

Purchase of Gas

Cost of natural gas purchased during the year was $31,254,750 compared to $20,516,544 last year. While the increased cost of gas is partly attributable to increased volumes purchased, it is largely due to the wholesale price increases referred to previously. The winter was warmer than normal and therefore large volumes of peaking gas were not required. Nevertheless, the East Kootenay Link was utilized to bring in some peak shaving gas from Alberta, thereby minimizing demand charges and improving the load factor of gas purchased from our major supplier, Westcoast.

Operation, Maintenance, Selling and Administrative

During the year operation and maintenance expenses amounted to $3,511,825 and selling, general and administrative expenditures were $1,751,162. The comparable figures for the previous year were $2,733,628 and $1,561,415 respectively. The increasing complexity of the transmission and distribution system coupled with major increases in the wholesale price of natural gas over the past few years has necessitated the installation of highly sophisticated gas control equipment and compressor stations, and has required the addition of skilled personnel for the constant operation of these facilities. The cost of operating the Company's gate station heaters and compressor stations has also increased materially due to the wholesale price increase of gas purchased to fuel these operations.

Additions to the Company's overall work force together with higher wage rates has increased the cost of salaries, wages and related employee benefits by 23% over the

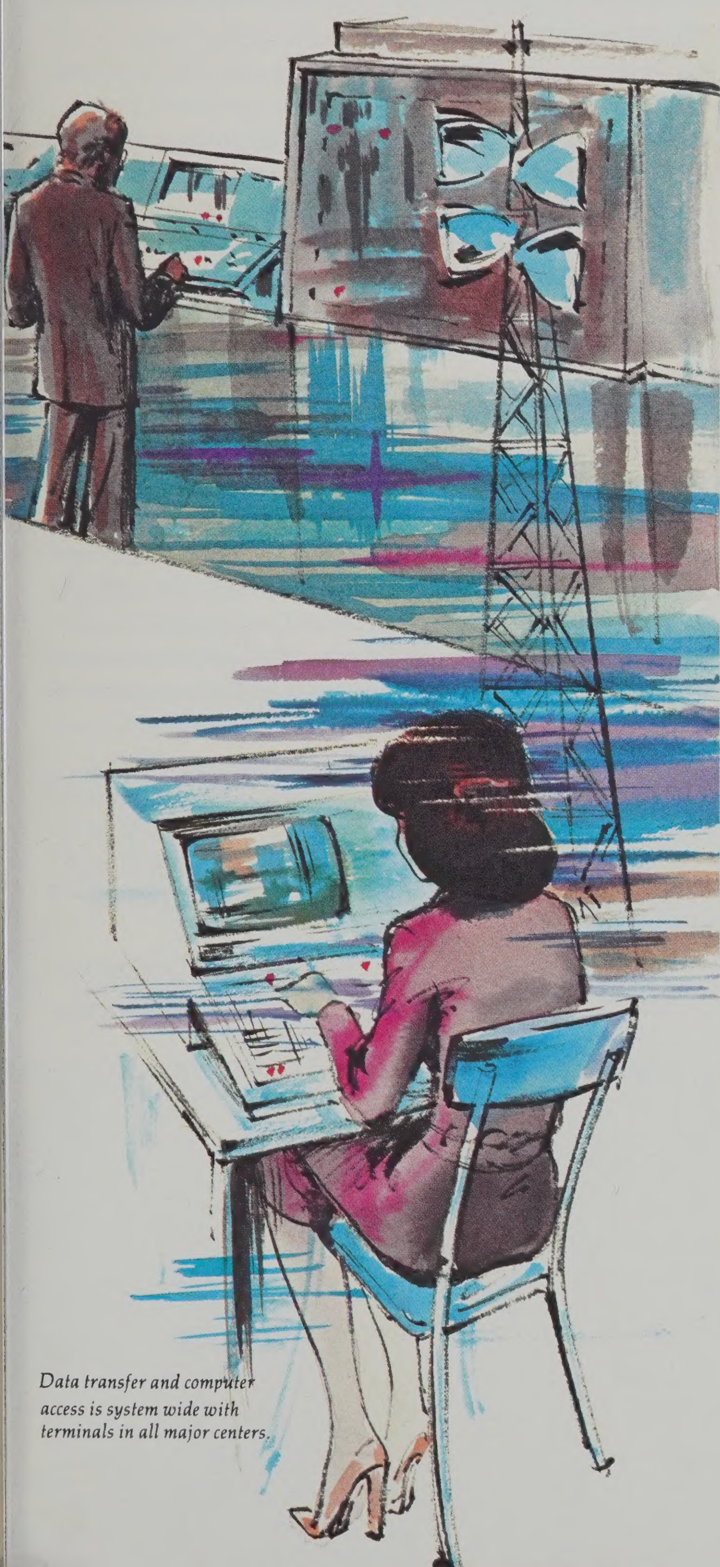
previous year to a total of almost $6 million. Not all of this increase, however, is charged to operating accounts as the Company's own work force is utilized to a large extent in the construction of new plant additions. Accordingly, a substantial portion of employee remuneration and related administrative costs are capitalized. While certain of the cost increases are difficult to control, the Company continues to strive for improved efficiencies and economies in its operations wherever possible.

The average number of employees on the payroll during the year was 271 compared to 249 a year ago. Approximately 75% of Company personnel are union members who are covered by two separate collective agreements, one with the Office & Technical Employees Union, and the other with the International Brotherhood of Electrical Workers. The agreement with the Office & Technical Employees Union expired on March 31, 1977 and the agreement with the International Brotherhood of Electrical Workers expired on September 11, 1977. Negotiations for new contracts are underway with each union.

Property, Franchise and Other Taxes

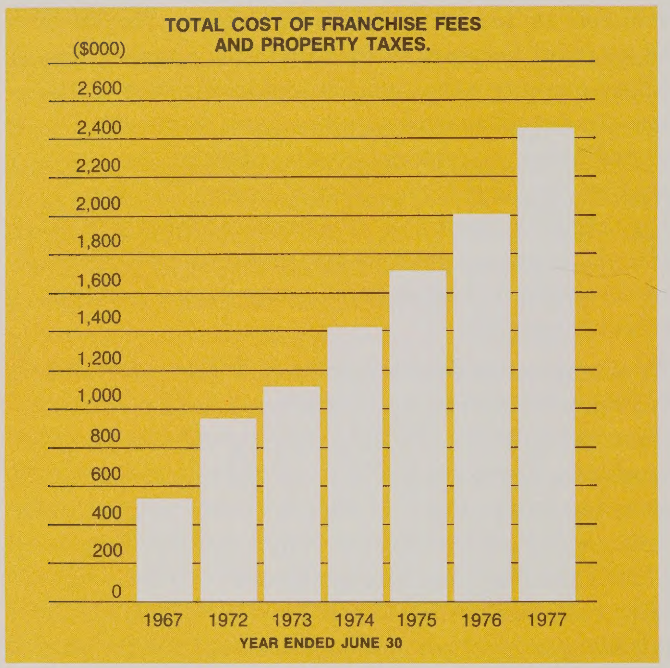
Your Company has contributed during the year $2,461,010 to the revenue of the municipalities it serves in the form of property taxes and franchise fees. Franchise fees alone amounted to $1,253,327 and reflect an increase of 36% over the previous year. The franchise fees are calculated at 3% of the total gross revenue from sales of natural gas within municipal boundaries. The significant increase in the wholesale and resulting retail price of natural gas, together with the increase in volume of sales over the past year, has given rise to the increase.

The B.C. Energy Commission has announced that an inquiry will be held on October 4, 1977 into the matter of franchise fees paid to municipalities by gas utilities in the province. The Commission is concerned that the matter of franchise fees be better understood and that a determination be made as to whether or not such fees are in the public interest and if so, how they should be administered. Your Company will be present at this inquiry to adduce evidence and to cross-examine witnesses.



Data transfer and computer access is system wide with terminals in all major centers.

Directors' Report



During the year, the Provincial corporation capital tax amounted to $106,779, a reduction of approximately 10% over the previous year.

Depreciation

The table below sets out depreciation rates for major plant classifications:

Transmission and distribution mains	2%
Meters, compressors, buildings, measuring and regulating equipment	3%
Other general equipment	5% to 15%

The composite depreciation rate was 2.30%. This rate was slightly lower than the rate in the previous year due to the placing in service of the East Kootenay Link; this major addition to transmission plant attracts a 2% depreciation rate. Consolidated depreciation in fiscal 1977 amounted to $2,322,557 compared to $1,818,970 last year.

Interest and Expense on Long-Term Debt

Interest and expense on long-term debt amounted to $3,979,270 compared to $4,166,524 in the previous year. This decrease results from redemption, by way of short-term borrowings, of the 5½% Series "A" Convertible Sinking Fund Debentures which matured on February 15, 1977.

Other Interest

During the year, short-term capital was obtained from bank loans and the issuance of the Company's own commercial paper. Other interest amounted to $568,512 compared to $888,540 last year. The reduction was due to a lower level of short-term borrowings as a result of obtaining long-term capital by the $10 million issue of Second Preference Shares in June of 1976, and a decrease in the average interest rate from 9.81% to 8.40%.

Income Taxes

Income taxes for the current year were $1,671,651 compared to $250,036 in the previous year. The substantial increase in income taxes resulted primarily from the additional taxable revenue derived from the 7¢ interim increase which was in effect during all of fiscal 1977 but only half of fiscal 1976. In addition, as noted in the calculation set out below, there were decreases in the deductions from net income this year relating to non-taxable interest during construction, and timing differences. These changes resulted from the completion of the East Kootenay Link in the previous year and the commencement of depreciation on this pipeline in the current year.

	($000's) 1977	1976
Net income before taxes (Inland)	**$6,987**	$4,983
Deduct:		
Interest during construction	**31**	564
Excess C.C.A. and other timing differences	**3,669**	3,891
Other items (net)	**133**	69
	$3,154	$ 459
Effective tax rate	**51.00%**	50.49%
Income taxes —		
Inland	**$1,616**	$ 213
Subsidiaries	**56**	37
	$1,672	$ 250

Interest Charged to Construction

The Company follows the practice of capitalizing interest on funds used during construction of major plant additions. Interest charged to construction in the current year amounted to $30,682 compared to $563,583 in the previous year. Last year's high level of interest during construction resulted from the use of funds for construction of the East Kootenay Link.

FINANCING

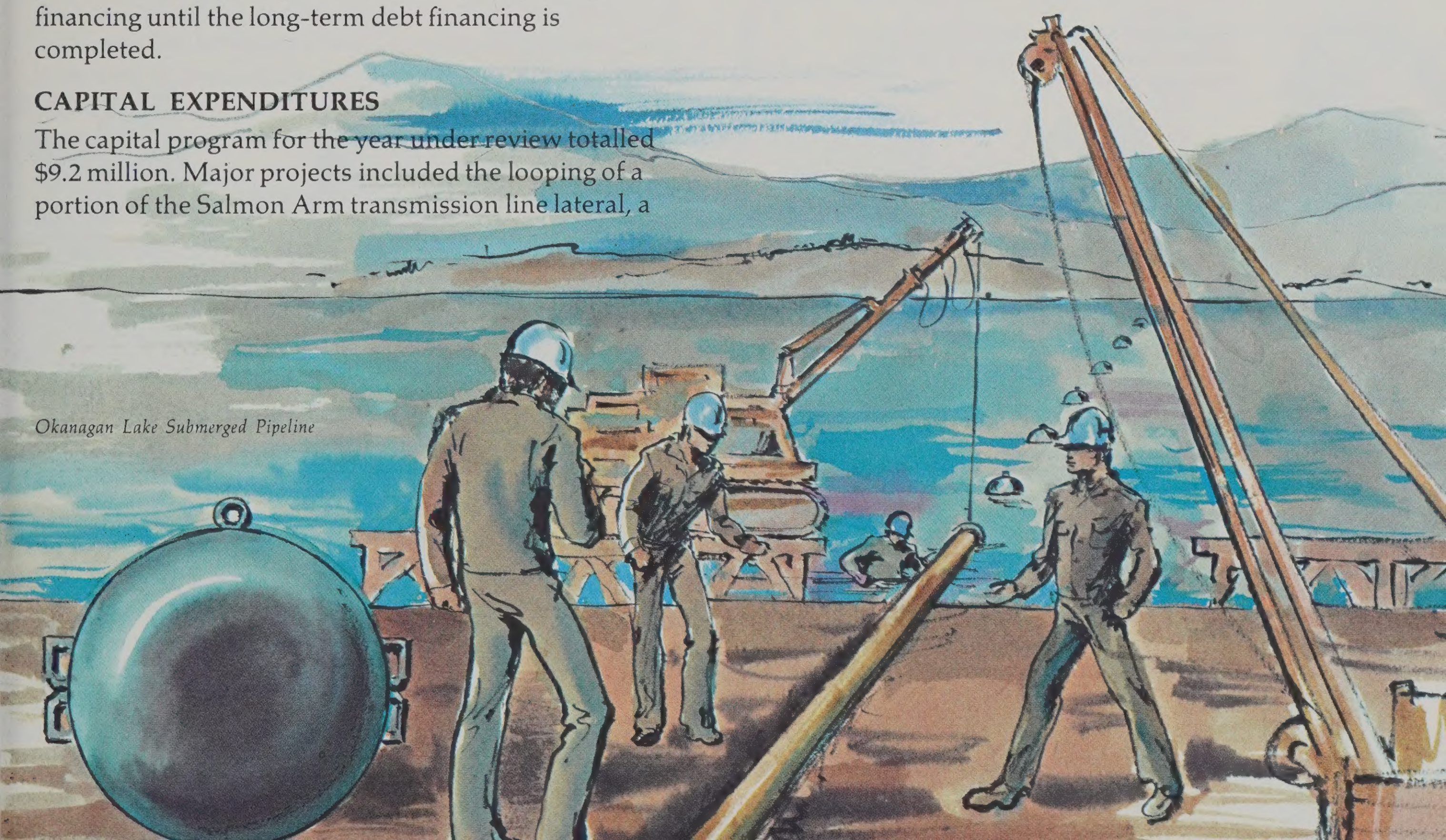
There were no financings carried out during the year under review. The Company is presently in the preliminary stages of preparation for an issue of long-term debt which will probably come to market in November of this year. The terms, conditions and size of the issue have not yet been determined. The Company has established lines of credit with its corporate bankers which enables it to utilize either bank loans or its own commercial paper. These funds, along with internally generated funds, will provide the necessary bridge financing until the long-term debt financing is completed.

CAPITAL EXPENDITURES

The capital program for the year under review totalled $9.2 million. Major projects included the looping of a portion of the Salmon Arm transmission line lateral, a new office building in Kelowna, and the final clean-up of the East Kootenay Link pipeline project. The submerged pipeline crossing of Okanagan Lake at Kelowna was also substantially completed during the year and will be put in service in the fall of 1977. This facility provides for additional gas requirements to the Westbank and Lakeview Heights area.

FUTURE CAPITAL EXPENDITURES

There are relatively few major projects in the Company's $8 million capital program for the coming year. The budget includes the installation of a second 1100 HP compressor unit at the Trail compressor station, a new meter station to serve additional gas requirements at Intercontinental Pulp Company Ltd. and Prince George Pulp and Paper Limited, and some transmission line reinforcement in the Kamloops area. Also provided for are routine expenditures for the installation of facilities to serve an estimated 3,500 new customers.



Okanagan Lake Submerged Pipeline

Directors' Report

RATES & REGULATIONS

When your Company commenced operations in the fall of 1957 its original residential and commercial rates were only slightly lower than the competing cost of light oil. Over the years we have worked diligently to attract customers both from new construction and by way of conversions. These efforts have resulted in an increase in customers from 6,000 initially, to over 70,000 today. During these years management policies have incorporated the highest and most up-to-date operating practices, but always with the economics of our customers and a reasonable return to shareholders in mind. The average number of employees on the payroll in fiscal 1958, the Company's first year of operation, was 235. Today, nineteen years later, the average number of employees stands at 271. The Company's aggressive marketing approach and its economic operating policies, resulted over the years in six separate rate reductions to residential and commercial customers. Between the years 1965 to 1973 the average price paid by residential customers dropped from approximately $1.50 per Mcf to slightly under $1.00 per Mcf, while the comparative cost of light oil rose to a price approximately equivalent to $1.80 per Mcf.

These retail rates have since risen considerably because of wholesale price increases beyond the control of the Company, which were passed on to consumers with the consent of the B.C. Energy Commission with no resulting profit to Inland. In spite of every effort made to combat the effect of inflation on operating costs, plant additions, and the cost of capital, it was finally necessary to apply for the first time for rate relief to preserve the financial integrity of the Company.

Interim rate relief was sought in the fall of 1975 and a 7¢ per Mcf refundable interim rate increase to all customer classes was granted effective January 2, 1976. The Company filed an application for permanent rate relief along with supporting material on January 31, 1977. The application requested new rates to all customer classifications, which would have added 27¢ per Mcf

Executive Vice-President, R. B. Stokes (below left) and Chief Engineer, G. M. O. Solly, at B.C. Energy Commission Hearings.

inclusive of the 7¢ per Mcf interim increase to the existing rates. The proposed increase to residential customers amounted to only roughly one-half of the rate reductions that had taken place over previous years. The Company, through its expert witnesses, testified that a rate of return on rate base of approximately 11% was reasonable considering the Company's cost of capital, and was consistent with recent returns experienced by the Company and reported to the regulatory body. The application also requested approval of certain accounting changes. These changes involved accounting for income tax on a normalized basis rather than the previously utilized flow-through method, additional depreciation charges, and a change in the method of allocating overhead costs between plant and operating accounts. Public hearings commenced on May 2, 1977 in Kelowna, and concluded on June 9, 1977 in Vancouver, and the Commission's decision was issued on August 31, 1977. The Commission in its decision has approved the change in income tax treatment to the normalized method and additional depreciation effective July 1, 1977, and has authorized the Company to introduce the proposed changes in the treatment of overhead costs effective July 1, 1978. The Commission also reduced the Company's rate base primarily in the area of working capital allowances.

The decision allows the Company a return on rate base of 10%, which according to the Commission results in approximately a 14% return on equity. In its decision, however, the Commission points out that it will contemplate no action to reduce tariffs should the return on equity rise to something in the order of 16%.

New rates were filed and became effective September 1, 1977, which add 9¢ per Mcf to residential and commercial rates and approximately 2¢ per Mcf to industrial rates over and above the 7¢ per Mcf interim which has been confirmed by the Commission. The new average price to residential customers will now be approximately $1.83 per Mcf which is approximately one-half of today's equivalent price of light oil.

ENERGY CONSERVATION

Your Company continues to promote the philosophy that Canadians must use all forms of energy wisely. To this end we will continue to support energy conservation programs sponsored by the Federal and Provincial Governments. Inland offers its customers a complete library of publications issued by the Department of Energy Conservation. Themes for home product exhibits and office displays stress the need to conserve energy. This same theme is found in consumer advertising, our school program, and presentations made to interested groups in our service area.

SHARE DISTRIBUTION

Approximately 95% of the shareholders of Preference and Common stock of the Company are resident in Canada. The distribution of each class of shares is set out below:

	Shareholders	Shares
Preference		
Canada	3,015	798,147
U.S.A.	14	1,178
Others	7	675
	3,036	800,000
Common		
Canada	4,552	2,532,993
U.S.A.	249	68,901
Others	74	220,228
	4,875	2,822,122

WHOLLY-OWNED SUBSIDIARIES

Peace River Transmission Company Limited

The Company is an Inter-Provincial pipeline company and is subject to regulation by the National Energy Board. It purchases natural gas from Westcoast Transmission Company Limited and delivers it to the outskirts of the City of Dawson Creek in northeastern British Columbia where it is sold to Northland Utilities (B.C.) Limited for distribution in Dawson Creek and the surrounding area.

Natural gas sales volume for the year under review was 1,029,558 Mcf compared to 1,107,015 Mcf in the previous year. The abnormally mild winter resulted in a slight decrease in sales. Net income for the year was $33,201 compared to $35,491 in fiscal 1976.

Directors' Report

Grande Prairie Transmission Co. Ltd.

The Company is incorporated under the laws of the Province of Alberta and is subject to regulation by the Public Utilities Board of Alberta. It purchases natural gas from producers at various fields north of Grande Prairie in the Peace River area of Alberta and transmits it for resale by Northwestern Utilities Limited to the City of Grande Prairie and other communities in the immediate area.

Gas sales volume for the year under review was 1,967,496 Mcf which was slightly down from last year's sales of 1,996,365 Mcf, due to the exceptionally mild winter throughout this area. The Company experienced a loss of $15,792 for the year compared to a profit last year of $8,503.

During the year two producing wells were abandoned, but at the present time arrangements are in hand to tie-in two new wells in the immediate vicinity of our pipeline. Drilling in the immediate area is still active and any new wells within economic distance of our pipeline will be investigated and the gas contracted for, as and when required.

St. John Gas & Oil Co. Ltd. (NPL)

This subsidiary holds minor interests in natural gas and oil leases in northeastern British Columbia and participates in the production of natural gas and oil from these leases. Net loss for the year amounted to $15,492 after providing for the write-off of unproductive exploration expenses amounting to $20,876.

Inland Development Co. Ltd.

This subsidiary owns property in the Okanagan Valley. During the year under review, the Company sold its office building in the City of Kelowna, and recorded a profit of $136,835.

TO OUR EMPLOYEES

Although Inland Natural Gas Co. Ltd. was incorporated twenty-five years ago, the Company did not engage significant numbers of employees until the commencement of operations in 1957. At that time, your Company was fortunate to attract a group of well qualified technical and managerial people who accepted the challenge offered by a young company in a growing service area. These original employees and the employees who joined the Company in its ensuing years helped provide the environment for the continuous growth that has taken place since the beginning of the Company.

Seventy-four of the present day work force have been with the Company for more than ten years. Twenty-five of those employees have been with the Company since 1957.

Since the commencement of operations in 1957, personnel have played a very important role in the Company's development. Inland employees have always participated in a wide range of off-the-job activities such as Trade Associations, Chambers of Commerce, Boards of Trade, sports, youth groups, service clubs and numerous other volunteer community agencies. This community involvement has not only stimulated sales but has also created valuable goodwill within our service area.

The Board of Directors would like to record its recognition of all Inland employees whose personal involvement and dedication have made a major contribution to the growth of the Company.

For the Board of Directors

R. Laudcliff

Chairman of the Board

September 28, 1977

Consolidated Statement of Income

For the year ended June 30

	1977	1976
REVENUE		
Sale of gas	**$51,621,709**	$37,471,711
Transportation revenue	**825,950**	296,700
Other operating revenue	**646,216**	528,355
	53,093,875	38,296,766
EXPENSES		
Purchase of gas	**31,254,750**	20,516,544
Operation and maintenance	**3,511,825**	2,733,628
Selling, general and administrative	**1,751,162**	1,561,415
Property, franchise and other taxes	**2,567,789**	2,118,775
Depreciation	**2,322,557**	1,818,970
Interest and expense on long-term debt	**3,979,270**	4,166,524
Other interest	**568,512**	888,540
Interest charged to construction	**(30,682)**	(563,583)
	45,925,183	33,240,813
Income before income taxes	**7,168,692**	5,055,953
Income taxes	**1,671,651**	250,036
NET INCOME	**$ 5,497,041**	$ 4,805,917
EARNINGS PER COMMON SHARE, after provision for preference dividends	**$ 1.44**	$ 1.56

Consolidated Statement of Retained Earnings

For the year ended June 30

	1977	1976
BALANCE AT BEGINNING OF YEAR	**$14,864,683**	$12,729,121
Net income	**5,497,041**	4,805,917
	20,361,724	17,535,038
Dividends on 5% preference shares	**400,000**	400,000
Dividends on 10% second preference shares	**1,044,000**	—
Dividends on common shares—$.80 per share	**2,257,698**	2,257,698
Amortization of preference share issue costs	**31,758**	12,657
	3,733,456	2,670,355
BALANCE AT END OF YEAR	**$16,628,268**	$14,864,683

See accompanying summary of accounting policies and notes.

Consolidated
As at

Assets

	1977	1976
CURRENT ASSETS		
Accounts receivable	$ 5,577,447	$ 4,434,365
Inventories of construction and operating materials and supplies, at cost	1,799,239	1,451,421
Prepaid expenses	254,773	221,375
	7,631,459	6,107,161
NON-CURRENT ASSETS		
Mortgages and other long-term receivables	141,741	100,668
Investment in marketable securities, at cost (quoted market 1977—$103,000; 1976—$87,000)	100,000	100,000
Real estate held for resale, at cost	823,879	757,864
	1,065,620	958,532
PROPERTY, PLANT AND EQUIPMENT, at cost		
Natural gas transmission lines and distribution systems	103,199,721	97,666,901
Plant, buildings and equipment	5,510,850	5,014,157
Land and land rights	1,996,405	2,065,815
Construction work in process	1,859,849	461,077
	112,566,825	105,207,950
Accumulated depreciation	16,425,066	14,578,877
	96,141,759	90,629,073
Interest in petroleum and natural gas properties	172,902	169,949
Accumulated depletion	63,420	62,970
	109,482	106,979
	96,251,241	90,736,052
OTHER ASSETS AND DEFERRED CHARGES		
Unamortized preference share issue costs	1,390,460	1,431,220
Unamortized long-term debt issue costs	779,506	939,805
Unamortized rate hearing costs	254,377	—
	2,424,343	2,371,025
	$107,372,663	$100,172,770

See accompanying summary of accounting policies and notes.

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Liabilities

CURRENT LIABILITIES	1977	1976
Bank loan and short-term notes	**$ 10,714,737**	$ 1,186,938
Accounts payable	**4,564,324**	4,790,107
Dividends payable	**350,000**	100,000
Income taxes	**1,389,456**	204,606
Property, franchise and other taxes accrued	**2,420,676**	2,056,927
Interest accrued on long-term debt	**423,917**	522,103
Current portion of long-term debt	**599,395**	4,620,220
	20,462,505	13,480,901
LONG-TERM DEBT (Note 1)	**43,976,550**	45,521,846

Shareholders' Equity

CAPITAL STOCK (Note 2)		
5% Cumulative redeemable preference shares, par value $20 per share Authorized and issued: 400,000 shares	**8,000,000**	8,000,000
10% Cumulative redeemable second preference shares, par value $25 per share Authorized and issued: 400,000 shares	**10,000,000**	10,000,000
Common shares, par value $1 per share Authorized: 5,000,000 shares Issued: 2,822,122 shares	**2,822,122**	2,822,122
PREMIUM ON COMMON SHARES	**5,483,218**	5,483,218
RETAINED EARNINGS (Note 3)	**16,628,268**	14,864,683
	42,933,608	41,170,023
	$107,372,663	$100,172,770

Approved on behalf of the Board

Director R. Laidlaw

Director [signature]

Consolidated Statement of Changes in Financial Position

For the year ended June 30

	1977	1976
SOURCE OF WORKING CAPITAL		
Operations		
Net income	$ 5,497,041	$ 4,805,917
Items not involving working capital		
Depreciation and amortization	2,362,196	1,873,635
Other	(258,846)	(109,000)
Total from operations	7,600,391	6,570,552
Second preference shares issued	—	10,000,000
Other — net	609,990	204,387
	8,210,381	16,774,939
APPLICATION OF WORKING CAPITAL		
Additions to property, plant and equipment	8,257,079	14,392,029
Dividends on preference and common shares	3,701,698	2,657,698
Reduction of long-term debt	1,454,533	5,290,228
Second preference share issue costs	—	393,921
Rate hearing costs	254,377	—
	13,667,687	22,733,876
DECREASE IN WORKING CAPITAL	5,457,306	5,958,937
Working capital deficit at beginning of year	7,373,740	1,414,803
WORKING CAPITAL DEFICIT AT END OF YEAR	$ 12,831,046	$ 7,373,740

See accompanying summary of accounting policies and notes.

To the Shareholders
Inland Natural Gas Co. Ltd.

AUDITORS' REPORT

We have examined the consolidated balance sheet of Inland Natural Gas Co. Ltd. as at June 30, 1977 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at June 30, 1977 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Vancouver, B.C.
August 31, 1977

Thorne Riddell & Co.
Chartered Accountants

Summary of Accounting Policies

The Company and its transmission subsidiaries are regulated utilities and their accounting records and practices conform to the requirements of their respective regulatory authority. Significant accounting policies are set out below:

Principles of Consolidation
The consolidated financial statements include the accounts of Inland Natural Gas Co. Ltd. and its subsidiaries Peace River Transmission Company Limited, Grande Prairie Transmission Co. Ltd., Inland Development Co. Ltd., St. John Gas & Oil Co. Ltd. (N.P.L.), Inland Transmission Co. Ltd. and Inland Development (1957) Co. Ltd., all of which are wholly-owned.

Property, Plant and Equipment
The cost of utility plant additions, major renewals and betterments, including direct costs, general and administrative costs allocable to construction and interest on funds used during construction are capitalized. The cost of depreciable utility plant retired together with removal costs less salvage is charged to accumulated depreciation. Maintenance and repair costs of a routine nature are charged to expense as incurred.

Depreciation
Depreciation of plant in service is computed on a straight-line basis whereby rates for each class of plant, designed to amortize the cost of the assets over their estimated useful lives, are applied to the Company's investment in such plant at the beginning of the year. The application of these rates for the year ended June 30, 1977 results in a composite rate of 2.30%. Rates for major plant classifications are as follows:

Transmission and distribution mains	2%
Meters, compressors, buildings, measuring and regulating equipment	3%
General equipment	5% to 15%

Other Assets and Deferred Charges
Long-term debt issue costs are amortized over the original lives of the related debt. Gains on purchase of debt securities for sinking funds are amortized over the remaining lives of the related debt as a reduction of debt charges.

5% Preference share issue costs are amortized to retained earnings at the prescribed annual rate of 1%.

10% Second preference share issue costs are amortized to retained earnings over a 21 year period commencing July 1, 1976.

In accordance with the decision dated August 31, 1977 from the British Columbia Energy Commission, the majority of rate hearing costs are to be amortized over two years commencing July 1, 1977 and the balance amounting to $129,186 over a ten year period.

Income Taxes
The companies claim capital cost allowance and certain other deductions for income tax purposes in excess of the related amounts recorded as expense in their accounts, thereby reducing income taxes which would otherwise have been charged against income by $1,863,000 for the 1977 fiscal year and $16,787,000 in total to June 30, 1977. Since only the taxes currently payable are claimed for regulatory purposes in setting consumer rates, as has been approved by the companies' regulatory authorities, the companies follow the taxes payable basis and make no provision for such reductions.

The Company's application to amend its tariffs included a request to change the method of accounting for income taxes in its accounts and for regulatory purposes from the taxes payable (flow-through) basis to the deferred tax allocation (normalized) basis and to recover such additional taxes concurrently in rates charged to customers. The decision from the British Columbia Energy Commission dated August 31, 1977 instructs the Company to introduce deferred income taxes into its accounting system in the year ended June 30, 1978 and to continue to recognize the unrecorded tax allocation balance which has accumulated in prior years by note to the financial statements.

Pension Plan

The companies have pension plans for their employees which have been revised and amended from time to time. The plans require that actuarial studies be prepared every three years. The most recent actuarial valuations were prepared as at January 1, 1976 for the plan for salaried employees and as at April 1, 1976 for the plan for other employees. Reports from the actuaries indicate that there are no unfunded liabilities for past service benefits.

Earnings Per Common Share

Earnings per common share are calculated using the weighted monthly average number of shares outstanding during the respective fiscal years. Dividend requirements on preference shares of $1,444,000 in 1977 and $400,000 in 1976 are deducted from net income for purposes of these calculations.

There would be no material dilution of earnings per share if the outstanding common share purchase warrants had been exercised during the year.

Notes to Consolidated Financial Statements

1. Long-Term Debt

	Total Outstanding	Current Liability	Long-Term 1977	Long-Term 1976
Inland Natural Gas Co. Ltd.				
First mortgage sinking fund bonds				
6¼% Series C, due May 1, 1983	$13,456,000	$108,000	$13,348,000	$14,066,000
8% Series D, due December 31, 1989	4,566,000	109,000	4,457,000	4,566,000
8¼% Series E, due November 1, 1991	7,110,000	—	7,110,000	7,250,000
8⅜% Series F, due April 15, 1993	7,380,000	130,000	7,250,000	7,380,000
11⅛% Series G, due June 15, 1995	11,835,000	185,000	11,650,000	11,835,000
	44,347,000	532,000	43,815,000	45,097,000
Inland Development Co. Ltd.				
9% Mortgage, repayable in monthly instalments of $2,001 based on a 20 year term to 1991	—	—	—	195,901
9% Mortgage, repayable in annual instalments of: 1978—$88,000; 1979—$88,000; 1980—$96,017.	228,945	67,395	161,550	228,945
	$44,575,945	$599,395	$43,976,550	$45,521,846

The first mortgage bonds are secured by a Trust Deed which constitutes in favour of the Trustee a first, fixed and specific mortgage and charge of and upon certain property of the Company and a first floating charge on the undertaking and all other property and assets, present and future of the Company, in the manner and to the extent set forth in the Trust Deed.

The trust agreement relating to the bonds requires the Company to establish sinking funds to retire various amounts of each issue prior to maturity. The annual requirements to date have been fulfilled by retirement of the stipulated amount of such securities. Sinking fund requirements over the next five years, after giving effect to purchases and retirements as at June 30, 1977 are: 1978—$532,000; 1979—$1,380,000; 1980—$1,482,000; 1981—$1,598,000; 1982—$1,718,000.

2. Capital Stock

a) 5% Cumulative Redeemable Preference Shares

The 5% preference shares are redeemable at the option of the Company on thirty days notice at a price of $21 per share.

b) 10% Cumulative Redeemable Second Preference Shares

The 10% second preference shares are not redeemable before July 1, 1981 but will be redeemable thereafter at the option of the Company at a price of $26.25 per share if redeemed on or before June 30, 1982, and at prices reducing annually to $25 per share if redeemed after June 30, 1986.

The Company is required, in each calendar quarter commencing with the third calendar quarter of 1977, to purchase for cancellation 5,000 10% second preference shares in the open market at prices not exceeding $25 per share. If, in any calendar quarter, the Company is unable to purchase 5,000 shares, its purchase obligations carry over to succeeding calendar quarters for a total of 20,000 shares during each 12 month period ending June 30, after which date the Company has no further obligation to purchase shares for that period ending June 30.

c) Common Shares

The Series D bonds were issued with share purchase warrants which entitled holders to purchase common shares of the Company on or before June 15, 1979 at $17.50 per share, such price being subject to adjustment in certain events. On June 21, 1971 following the issue of common shares pursuant to the rights offering, the warrant exercise price was adjusted to $16.83 per share. 75,000 unissued shares have been reserved to meet this commitment.

3. Retained Earnings

The Trust Deed relating to the First Mortgage Sinking Fund Bonds contains certain restrictions upon the payment of dividends. At June 30, 1977 all of the Company's retained earnings were free of such restrictions.

4. Remuneration of Directors and Senior Officers

The aggregate direct remuneration paid by the Company to directors and senior officers for the year ended June 30, 1977 was $264,883 (1976—$242,850).

5. Anti-Inflation Act

The Company is subject to controls on dividends to the holders of the Company's common shares under the federal government's anti-inflation guidelines which became effective October 14, 1975.

6. Rate Matters

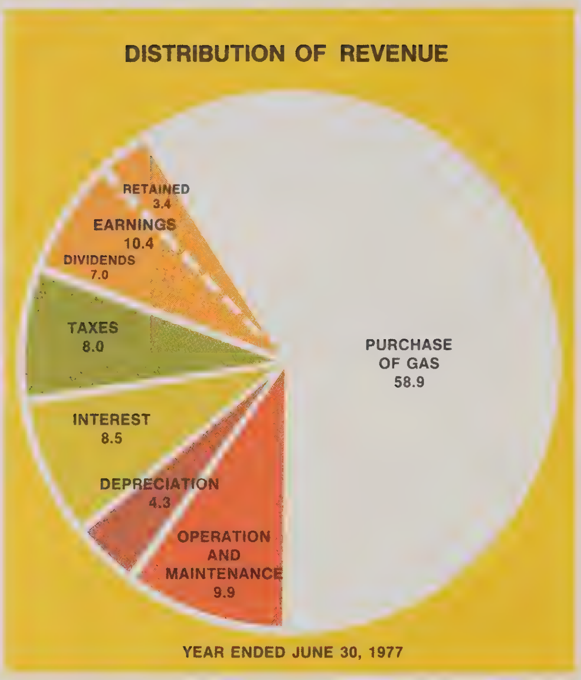
Pursuant to an application for interim rate relief the British Columbia Energy Commission, by orders dated January 1976, granted the Company an interim rate increase of 7¢ per Mcf to all classes of customers effective January 2, 1976. This increase was subject to refund with interest if so ordered by the Commission upon subsequent review of an application for permanent rate relief to be filed by the Company. On January 31, 1977, the Company filed an application to amend its tariffs, which application was heard before the Commission in public hearings in May and June. By an order dated August 31, 1977, the Commission found that the Company has justified the interim rate increase previously authorized and a further increase in rates effective for consumption of natural gas on and after September 1, 1977 or at the completion of any billing cycle then in progress.

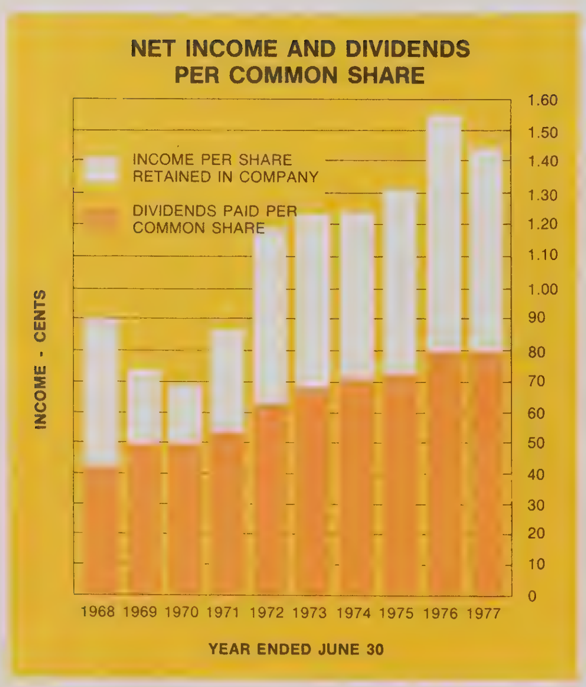
7. Capital Expenditures

Capital expenditures for 1978 are estimated at $8,000,000. Cash requirements will be provided by established corporate lines of credit together with cash from operations pending future financing.

8. Comparative Figures

Certain 1976 figures have been reclassified to conform with 1977 financial statement presentation.



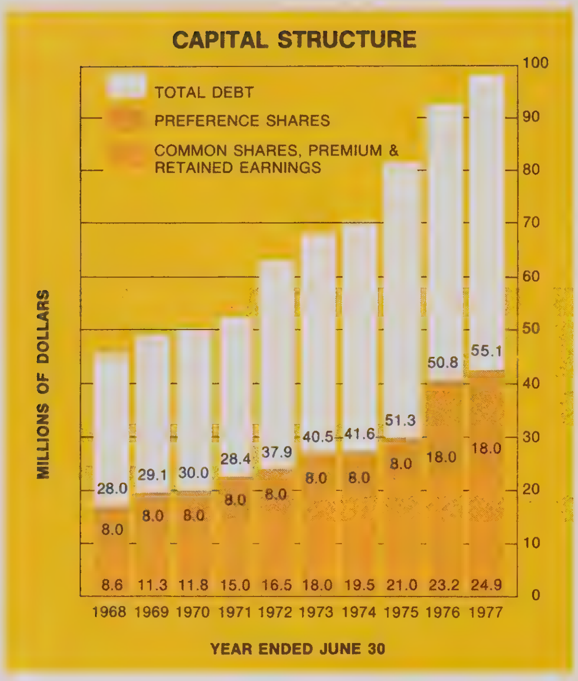


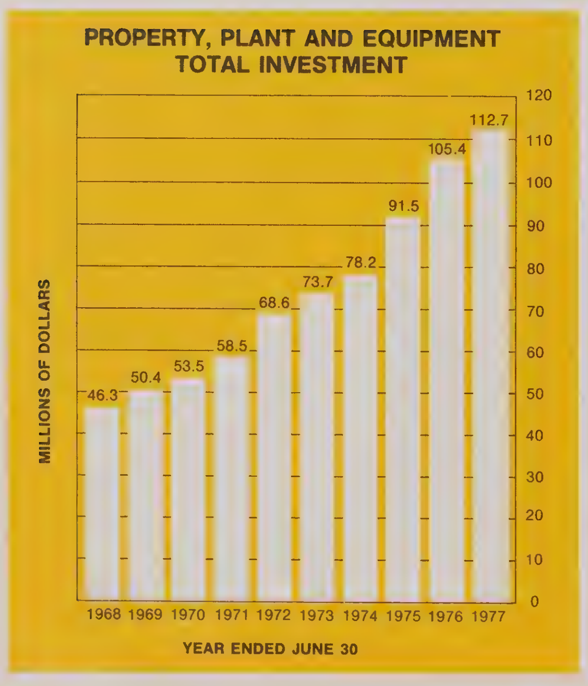
Comparative Statement c

	1977
REVENUE	
Sale of gas	$49,324,04
Transportation revenue	825,95
Other income	429,98
	50,579,97
EXPENSES	
Purchase of gas	29,515,46
Operation and maintenance	5,013,26
Property and other taxes	1,271,16
Franchise fees	1,253,32
Depreciation	2,240,40
Interest on borrowed money	4,505,88
Amortization of long-term debt issue costs	33,25
Interest charged to construction (credit)	(30,68
	43,802,07
INCOME BEFORE INCOME TAXES	6,777,90
Income Taxes	1,615,70
NET INCOME	5,162,19
Income from subsidiary companies (net)	334,84
NET CONSOLIDATED INCOME	$ 5,497,04
DIVIDENDS	
Preference shares	$ 1,444,00
Common shares	2,257,69
Total dividends	$ 3,701,69
NUMBER OF COMMON SHARES (average)	2,822,12
EARNINGS PER COMMON SHARE (after provision for preference dividends)	$ 1.4
DIVIDENDS PER COMMON SHARE	$ .8

Consolidated Income and Dividends

1976	1975	1974	1973	1972	1971	1970	1969	1968
5,786,016	32,414,184	27,272,202	22,664,204	18,269,877	15,544,855	14,146,424	13,960,737	12,545,300
296,700	296,700	296,700	288,880	260,023	234,030	229,032	199,400	151,800
445,086	328,971	488,703	352,712	331,191	242,211	219,627	259,489	275,416
6,527,802	33,039,855	28,057,605	23,305,796	18,861,091	16,021,096	14,595,083	14,419,626	12,972,516
9,423,365	18,663,501	14,155,016	10,403,343	8,117,278	6,949,267	6,650,914	6,702,964	5,971,774
4,042,170	3,197,242	2,723,477	2,382,680	2,015,214	1,713,627	1,655,258	1,764,769	1,486,372
1,153,879	920,547	791,251	650,950	541,075	475,903	430,785	386,764	346,214
922,528	839,649	649,628	455,525	381,973	333,279	258,094	257,692	211,725
1,732,656	1,661,278	1,554,102	1,447,087	1,192,131	1,154,571	1,037,895	965,584	916,347
4,982,241	3,678,765	3,019,393	2,662,467	2,331,595	1,956,895	1,948,695	1,791,638	1,708,993
54,665	47,009	60,190	63,323	67,179	67,157	74,994	97,625	97,215
(563,583)	(529,712)	(15,240)	(38,663)	(264,894)	(24,228)	(18,806)	(25,023)	(8,340)
1,747,921	28,478,279	22,937,817	18,026,712	14,381,551	12,626,471	12,037,829	11,942,013	10,730,300
4,779,881	4,561,576	5,119,788	5,279,084	4,479,540	3,394,625	2,557,254	2,477,613	2,242,216
212,678	703,700	1,446,269	1,495,561	994,769	956,362	594,511	490,580	—
4,567,203	3,857,876	3,673,519	3,783,523	3,484,771	2,438,263	1,962,743	1,987,033	2,242,216
238,714	236,357	216,009	99,708	281,130	207,694	179,306	215,613	275,547
4,805,917	4,094,233	3,889,528	3,883,231	3,765,901	2,645,957	2,142,049	2,202,646	2,517,763
400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000
2,257,698	2,088,370	2,031,928	1,947,264	1,777,937	1,414,514	1,285,921	1,228,367	995,191
2,657,698	2,488,370	2,431,928	2,347,264	2,177,937	1,814,514	1,685,921	1,628,367	1,395,191
2,822,122	2,822,122	2,822,122	2,822,122	2,822,122	2,578,100	2,571,843	2,437,550	2,341,625
1.56	1.31	1.24	1.23	1.19	.87	.68	.74	.90
.80	.74	.72	.69	.63	.55	.50	.50	.42½



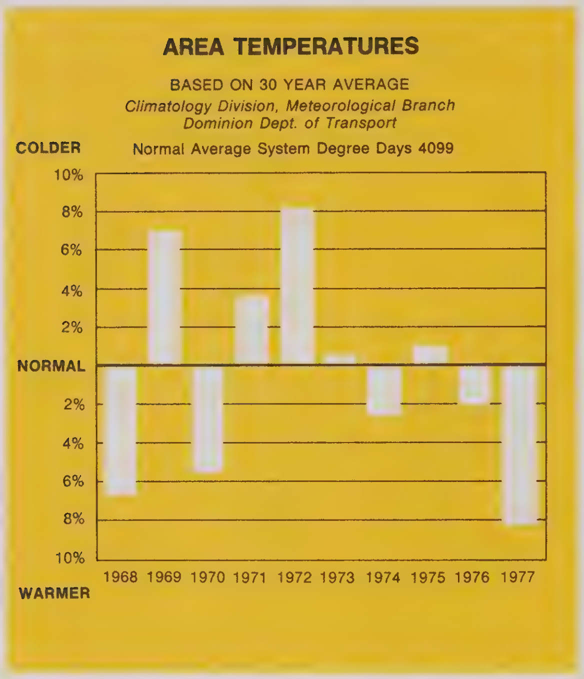


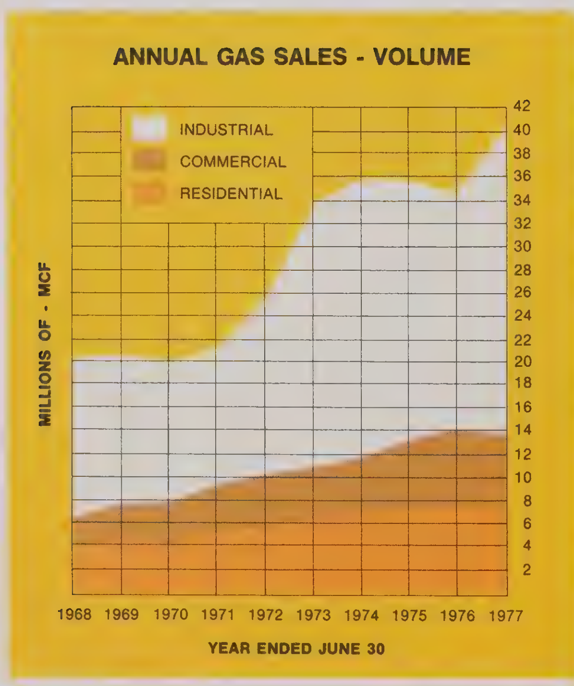
Consolidated Balanc

	197
MILES OF COMPANY OWNED LINES	
Transmission	90
Distribution	1,27
Services	98
Transmission-subsidiaries	12
UTILITY PLANT ($000)	
Transmission	$ 55,99
Distribution	47,77
Stand-by	88
General	2,85
Construction work in process	1,86
Total utility plant	109,36
SUBSIDIARIES' PLANT	3,37
	112,73
ACCUMULATED DEPRECIATION	
Inland Natural Gas Co. Ltd.	15,31
Subsidiary companies (including depletion)	1,17
	16,48
NET CONSOLIDATED PLANT	$ 96,25
CAPITALIZATION ($000)	
First mortgage bonds	$ 44,34
Debentures	—
Short-term notes and bank loan (net)	10,71
Total debt	55,06
Preference shares	18,00
Common shares	2,82
Premium on common shares	5,48
Retained earnings	16,62
	$ 97,99
PERCENT OF TOTAL CAPITALIZATION	
First mortgage bonds	45.
Debentures	—
Short-term notes and bank loan (net)	10.
Total percent of debt	56.
Preference shares	18.
Common shares	2.
Premium on common shares	5.
Retained earnings	17.
	100.
RATIOS	
First mortgage bond interest — times earned	3.0
Total debt interest — times earned	2.6
Preference dividends — times earned	3.81

Sheet Information

1976	1975	1974	1973	1972	1971	1970	1969	1968
889	816	781	777	769	624	603	559	481
1,211	1,141	1,082	1,000	898	831	778	691	626
937	871	814	740	671	614	569	526	491
122	122	116	116	115	115	115	115	115
53,981	34,839	34,047	33,190	31,680	22,552	22,330	21,046	19,062
43,613	39,322	36,374	33,000	29,558	26,820	25,420	23,005	21,510
882	882	882	883	913	364	364	362	361
2,728	2,671	2,601	2,537	2,528	2,597	2,605	2,522	2,197
461	10,095	739	618	591	3,499	134	896	615
101,665	87,809	74,643	70,228	65,270	55,832	50,853	47,831	43,745
3,713	3,711	3,517	3,470	3,343	2,708	2,688	2,570	2,512
105,378	91,520	78,160	73,698	68,613	58,540	53,541	50,401	46,257
13,494	12,106	10,594	9,267	8,225	7,277	6,615	5,726	4,862
1,148	1,066	989	912	844	788	733	680	632
14,642	13,172	11,583	10,179	9,069	8,065	7,348	6,406	5,494
90,736	78,348	66,577	63,519	59,544	50,475	46,193	43,995	40,763
45,498	46,277	35,137	35,810	28,960	21,943	22,567	23,478	18,894
4,151	4,151	4,384	4,623	4,879	5,110	5,360	5,600	5,840
1,187	863	2,116	76	4,071	1,300	2,031	—	3,258
50,836	51,291	41,637	40,509	37,910	28,353	29,958	29,078	27,992
18,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000
2,822	2,822	2,822	2,822	2,822	2,822	2,572	2,572	2,342
5,483	5,483	5,483	5,483	5,483	5,483	3,231	3,231	1,159
14,865	12,729	11,136	9,691	8,168	6,758	6,013	5,557	5,059
92,006	80,325	69,078	66,505	62,383	51,416	49,774	48,438	44,552
49.4	57.6	50.8	53.8	46.4	42.7	45.3	48.5	42.4
4.5	5.2	6.3	7.0	7.8	9.9	10.8	11.5	13.1
1.3	1.1	3.2	.1	6.5	2.5	4.1	—	7.3
55.2	63.9	60.3	60.9	60.7	55.1	60.2	60.0	62.8
19.6	10.0	11.6	12.0	12.8	15.5	16.1	16.5	18.0
3.1	3.5	4.1	4.2	4.5	5.5	5.1	5.3	5.2
5.9	6.8	7.9	8.3	8.8	10.7	6.5	6.7	2.6
16.2	15.8	16.1	14.6	13.2	13.2	12.1	11.5	11.4
100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
2.62	3.30	3.22	3.80	3.89	3.81	3.09	3.87	3.62
2.02	2.32	2.78	3.04	3.09	2.91	2.48	2.60	2.54
12.01	10.24	9.72	9.71	9.41	6.62	5.36	5.51	6.29





Comparative Statement of Sales

	197
REVENUE ($000)	
Residential	$12,46
Commercial	9,86
Small industrial	7,77
Large industrial and other	19,21
Total natural gas revenue	$49,32
SALES VOLUME (MMcf)	
Residential	7,44
Commercial	6,19
Small industrial	5,93
Large industrial and other	20,59
Total natural gas sales volume	40,17
CUSTOMERS AT YEAR END	
Residential	62,76
Commercial	8,58
Small industrial	10
Customers at year end	71,45
CUSTOMER STATISTICS	
Average use per customer (Mcf)	
Residential	12
Commercial	74
Average rate per Mcf	
Residential	$1.6
Commercial	1.5
COST OF NATURAL GAS PURCHASED ($000)	$29,51
VOLUME OF NATURAL GAS PURCHASED (MMcf)	39,76
MAXIMUM DAY SENDOUT (Mcf)	
Including interruptible	169,22
DEGREE DAYS (base 18°C.)	3,76
PAYROLL STATISTICS	
Wages and benefits ($000)	$5,99
Number of employees (average)	27

*excluding subsidiary companies

Purchases and Other Statistics*

1976	1975	1974	1973	1972	1971	1970	1969	1968
10,561	9,531	7,633	6,406	6,224	5,477	4,738	4,645	4,022
8,318	7,567	5,759	4,593	4,375	4,226	3,566	3,316	2,748
5,053	3,787	3,509	3,158	2,426	1,452	1,272	1,419	1,142
11,854	11,529	10,371	8,507	5,245	4,390	4,570	4,581	4,633
35,786	32,414	27,272	22,664	18,270	15,545	14,146	13,961	12,545
7,522	7,173	6,527	6,020	5,604	4,794	4,083	4,200	3,462
6,221	5,959	5,207	4,753	4,510	4,366	3,630	3,389	2,702
4,723	3,847	4,081	4,188	3,415	2,124	1,892	2,050	1,688
16,156	18,516	19,721	18,700	11,311	9,635	10,394	10,856	12,218
34,622	35,495	35,536	33,661	24,840	20,919	19,999	20,495	20,070
59,300	54,910	51,027	45,870	41,094	36,972	34,174	31,275	29,495
8,034	7,481	6,955	6,362	5,800	5,360	5,121	4,635	4,318
100	90	86	90	98	62	51	69	78
67,434	62,481	58,068	52,322	46,992	42,394	39,346	35,979	33,891
132	135	135	138	144	135	125	138	122
802	826	782	782	808	833	744	756	649
1.40	1.33	1.17	1.06	1.11	1.14	1.16	1.11	1.16
1.34	1.27	1.11	0.97	0.97	0.97	0.98	0.98	1.02
19,423	18,664	14,155	10,403	8,117	6,949	6,651	6,703	5,972
34,247	35,111	35,169	33,120	24,430	20,858	20,040	20,507	19,823
157,966	148,233	136,485	127,926	105,869	92,848	90,839	97,944	84,624
4,018	4,140	4,002	4,130	4,443	4,257	3,865	4,391	3,827
4,887	3,831	3,142	2,625	2,328	1,889	1,809	1,745	1,481
249	240	224	213	205	188	195	210	200

Communities Served

YEAR SERVICE COMMENCED	
1957	Quesnel
	Williams Lake
	100 Mile House
	Merritt
	Kamloops
	Armstrong
	Enderby
	Salmon Arm and Canoe
	Vernon
	Kelowna
	Summerland
	Penticton
	Oliver
	Osoyoos
	Grand Forks
	Rossland
	Trail and Tadanac
	Warfield
	Castlegar
	Nelson
1958	Chetwynd
	Prince George
1960	Shelley
1961	Oyama
1962	Lac La Hache
1964	Savona
	Winfield
	Okanagan Falls
1965	W.A.C. Bennett Damsite and Hudson Hope
	Robson
1967	Mackenzie
1968	Princeton
	Falkland
	Coldstream
	Peachland
	Westbank
	Naramata
	Midway
	Lakeview Heights
1969	Clinton
	Lumby
1971	Logan Lake
	Cache Creek
	Ashcroft
1972	Keremeos
1974	Hedley
1975	Salmo
	Fruitvale
	Montrose

R. E. Kadlec, President and Chief Operating Officer, addresses municipal convention.

Kootenay Link. As mentioned above, the Link has been in constant use transporting gas for Westcoast Transmission Company Limited and Columbia Natural Gas Limited.

Restatement of Prior Year's Income Taxes

In accordance with the Company's previous policy under the taxes payable method, income tax recoveries relating to tax losses, which resulted primarily from the claiming of excess capital cost allowances and other timing differences, were carried forward or backward to profitable quarters. Thus, the estimated tax losses for the June quarter were carried back to reduce taxes in the profitable March quarter.

As a result of the change in method of accounting for income taxes to the tax allocation basis (referred to in the September quarterly report to shareholders) and due to the interrelationship of timing differences in the calculation of current and deferred income taxes, the method of providing for current income taxes in interim periods has been changed to reflect tax recoveries in the respective unprofitable periods.

Income taxes for the corresponding period in 1977 have been restated to conform with this policy, and has resulted in a reduction of earnings per common share for the March 1977 quarter of 12¢, and a corresponding increase of 12¢ for the June 1977 quarter.

Outlook

The last quarter of the Company's fiscal year has traditionally shown a loss per common share. Last year, however, the Company earned 24¢ (restated) per common share in the quarter ending June 30, 1977. This unusual occurrence was largely brought about by the restatement of prior year's income taxes referred to above, a capital gain from the sale of property, and transportation revenue for the wheeling of gas for Westcoast. The Company does not anticipate any such revenues from the latter two sources in the final quarter this year.

For the Board of Directors

R. Lauchlan

Chairman of the Board

President

Vancouver, B.C.
May 8, 1978

INLAND
NATURAL GAS CO. LTD.

INTERIM REPORT
March 31, 1978

CONSOLIDATED COMPANIES	ACT OF INCORPORATION
Inland Natural Gas Co. Ltd.	Province of British Columbia Companies Act
Wholly-owned Subsidiaries	
Peace River Transmission Company Limited	Special Act of the Parliament of Canada
Grande Prairie Transmission Co. Ltd.	Province of Alberta Companies Act
Inland Development Co. Ltd.	Province of British Columbia Companies Act
St. John Gas & Oil Co. Ltd. (N.P.L.)	Province of British Columbia Companies Act
Inland Transmission Co. Ltd.	Province of British Columbia Companies Act
Inland Development (1957) Co. Ltd.	Province of British Columbia Companies Act

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Fold out for system map.

Communities Served

YEAR SERVICE COMMENCED

1957
1958
1960
1961
1962
1964
1965
1967
1968
1969
1971
1972
1974
1975

Montrose

INLAND NATURAL GAS CO. LTD. *and Wholly-owned Subsidiaries*

CONSOLIDATED STATEMENT OF INCOME

	Three Months Ended Mar. 31, 1978	Three Months Ended Mar. 31, 1977
REVENUE		
Sale of gas	**$22,440,590**	$16,716,673
Transportation revenue	**241,299**	463,782
Other operating revenue	**183,233**	107,821
	22,865,122	17,288,276
EXPENSES		
Purchase of gas	**13,705,877**	9,772,266
Operation, maintenance and administrative	**1,726,614**	1,491,101
Property, franchise and other taxes	**915,594**	746,561
Depreciation	**696,191**	584,231
Interest and expense on long-term debt	**1,221,519**	976,823
Other interest	**47,395**	189,340
Interest charged to construction	**(3,873)**	(9,308)
	18,309,317	13,751,014
Income before income taxes	**4,555,805**	3,537,262
Income taxes*		
Current	**1,914,607**	1,362,617
Deferred	**402,092**	—
	2,316,699	1,362,617
NET INCOME	**2,239,106**	2,174,645
Dividends declared on preference shares	**350,000**	350,000
	$ 1,889,106	$ 1,824,645
EARNINGS PER COMMON SHARE	**$ 0.67**	$ 0.65
Common shares outstanding on March 31st	**2,822,122**	2,822,122
Total gas sales volume (Mcf)		
- Inland	**13,265,774**	12,421,783
- Subsidiaries	**1,366,167**	1,135,561
	14,631,941	13,557,344

**See Report To Shareholders*

The above statement has been prepared from the books of account

Corporate Data

DIRECTORS

of the Board,
' Gas Co. Ltd.
ɔx Industries Ltd.
ɹc Mines Ltd.
ief Operating Officer,
ɹs Co. Ltd.

ɹs Co. Ltd.
ief Operating Officer,
ı Canada Limited
)kanagan Holdings Ltd.
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F INCORPORATION

ɔe of British Columbia Companies Act

Act of the Parliament of Canada
ɔe of Alberta Companies Act
ɔe of British Columbia Companies Act
ɔe of British Columbia Companies Act
ɔe of British Columbia Companies Act
ɔe of British Columbia Companies Act

Nine Months Ended Mar. 31, 1978	Mar. 31, 1977
$54,654,890	$39,664,043
879,070	612,132
393,233	369,327
55,927,193	40,645,502
34,067,924	23,337,860
4,449,931	4,006,014
2,318,749	1,930,786
2,062,689	1,743,270
3,254,496	3,037,945
502,599	377,104
(80,907)	(16,467)
46,575,481	34,416,512
9,351,712	6,228,990
3,345,278	1,750,024
1,345,100	—
4,690,378	1,750,024
4,661,334	4,478,966
1,050,000	1,094,000
$ 3,611,334	$ 3,384,966
$ 1.28	$ 1.20
2,822,122	2,822,122
34,263,403	31,903,180
3,060,397	2,488,813
37,323,800	34,391,993

s unaudited.

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Fold out for system map.

Communities Served

YEAR SERVICE COMMENCED

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1971	Lo
	Ca
	As
1972	Ke
1974	He
1975	Sal
	Fr
	Montrose

INLAND NATURAL GAS CO. LTD. *anc*

REVENUE
- Sale of gas
- Transportation revenue
- Other operating revenue

EXPENSES
- Purchase of gas
- Operation, maintenance and administrative
- Property, franchise and other taxes
- Depreciation
- Interest and expense on long-term debt
- Other interest
- Interest charged to construction

Income before income taxes

Income taxes*
- Current
- Deferred

NET INCOME

Dividends declared on preference shares

EARNINGS PER COMMON SHARE

Common shares outstanding on March 31st

Total gas sales volume (Mcf)
- Inland
- Subsidiaries

**See Report To Shareholders*

The above stat

TO OUR SHAREHOLDERS

Earnings

Comparative consolidated statements of income fo third quarter and the nine months ended March 31, 1 form part of this report. Earnings per common share ter provision for dividends on preference shares, creased during the quarter from 65¢ (restated) to and from $1.20 (restated) to $1.28 for the nine m period.

Common Share Dividends

We are pleased to report that by resolution dated A 18, 1978, the Directors of your Company declared Q terly Dividend No. 58 at the rate of 20¢ per com share payable on May 15, 1978 to shareholders of re at the close of business on April 28, 1978.

Revenue

Inland's sales volume for the nine months under re totalled 34,263,403 Mcf, an increase of 7.4% over same period last year. The increase was due in part t addition of approximately 3,000 residential and mercial customers, and weather that was slightly co than normal and considerably colder than experience the previous nine month period. The majority of th creased sales volume, however, resulted from sale Columbia Natural Gas Limited by way of the Kootenay Link. So far this year we have sold to Co bia approximately 2,600,000 Mcf compared to 800 Mcf last year. At the present time sales to Columbia ceased, and the possibility of any future sales will de upon the price to Columbia of their normal sourc Alberta gas relative to the price of gas available Inland. The increased volumes in the above menti categories were somewhat offset by lower sales to large industrial customers.

While sales volumes increased, the revenue from sales increased dramatically due to the flowing throug our customers of wholesale price increases during period under review. These price increases, of co resulted from increases in the wholesale cost of gas chased and result in no additional profit to the Comp

Transportation revenue has also increased. revenue is derived from the transportation of gas Westcoast Transmission Company Limited through East Kootenay Link as described in previous rep This transportation of gas from Westcoast has ceased, and whether it will materialize again next wi remains uncertain.

Expenses

Operation, maintenance and administrative expe have increased approximately 10% during the 9 mo under review. A significant portion of this increase i result of extended compressor station operation related costs due to the increased use of the

Corporate Data

DIRECTORS

+ *Ronald L. Cliff	Chairman of the Board, Inland Natural Gas Co. Ltd.
Roderick M. Hungerford	President, Flex-Lox Industries Ltd.
+ *J. Norman Hyland	President, Granduc Mines Ltd.
+ Robert E. Kadlec	President and Chief Operating Officer, Inland Natural Gas Co. Ltd.
Donald R. MacPhail	Secretary, Inland Natural Gas Co. Ltd.
Thomas G. Rust	President and Chief Operating Officer, Crown Zellerbach Canada Limited
*Horace B. Simpson	Vice-President, Okanagan Holdings Ltd.
+ Richard B. Stokes	Executive Vice-President, Inland Natural Gas Co. Ltd.
*H. Richard Whittall	Partner, Richardson Securities of Canada

+Member of the Executive Committee.
*Member of the Audit Committee.

All Directors reside in British Columbia.

OFFICERS

Ronald L. Cliff, C.A.	Chairman of the Board
Robert E. Kadlec, P.Eng.	President and Chief Operating Officer
Richard B. Stokes, C.A.	Executive Vice-President
Clifford I. Kleven, C.A.	Treasurer and Controller
Donald R. MacPhail, L.L.B.	Secretary
Ardelle F. Clark	Assistant Secretary

HEAD OFFICE

1075 West Georgia Street, Vancouver, B.C. V6E 3G3.

Approximately November 1, 1977, Inland Natural Gas Co. Ltd. will be relocating to 1066 West Hastings Street, Vancouver, B.C. V6E 3G3.

REGISTRAR

Canada Permanent Trust Company, Vancouver, B.C.

TRANSFER AGENT

Canada Permanent Trust Company,
Vancouver - Calgary - Toronto - Montreal - Halifax.

AUDITORS

Thorne Riddell & Co.

CONSOLIDATED COMPANIES	ACT OF INCORPORATION
Inland Natural Gas Co. Ltd.	Province of British Columbia Companies Act
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Inland Development Co. Ltd.	Province of British Columbia Companies Act
St. John Gas & Oil Co. Ltd. (N.P.L.)	Province of British Columbia Companies Act
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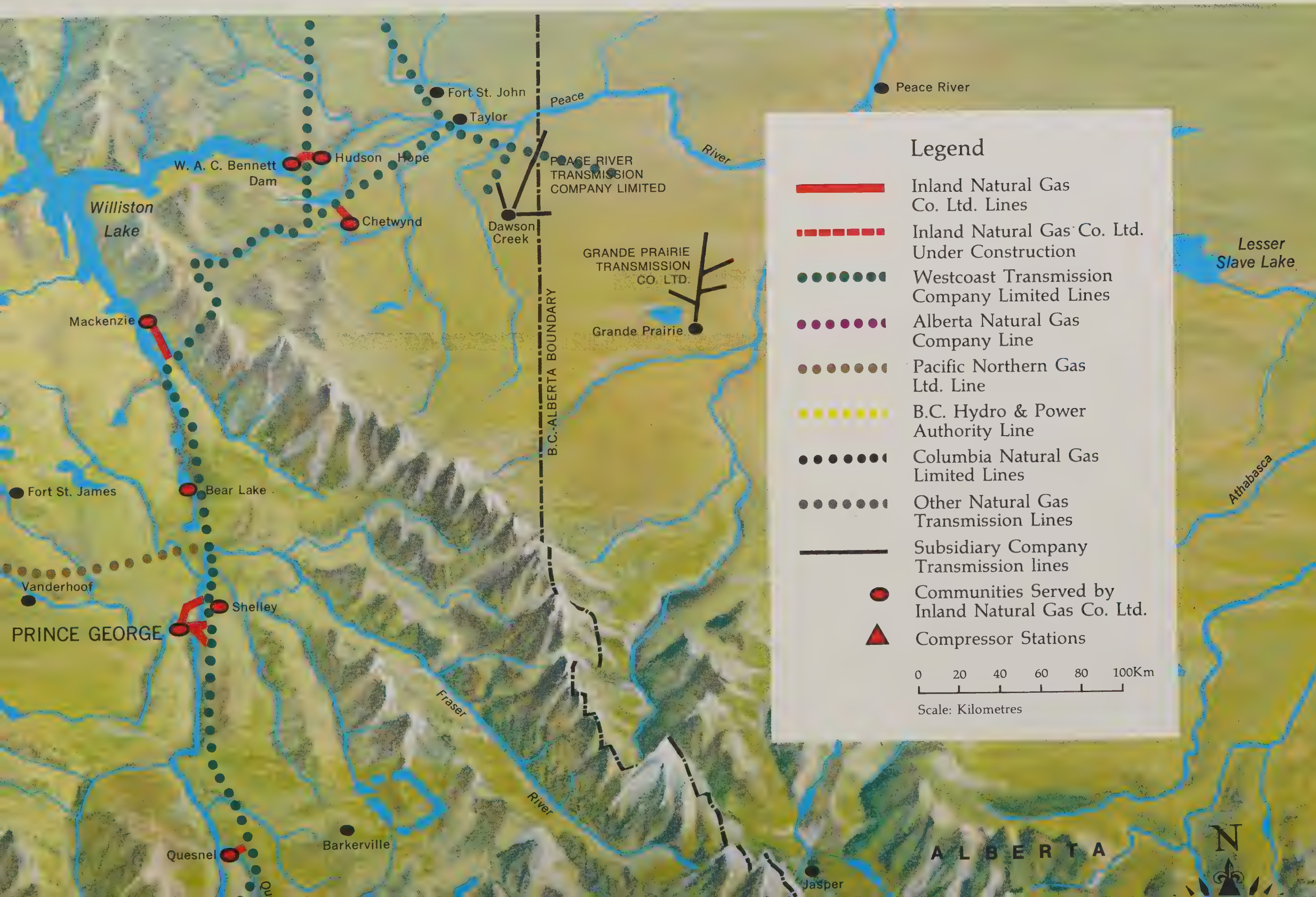
Fold out for system map.

INLAND NATURAL GAS CO. LTD. DISTRIBUTION AREA



BRITISH COLUMBIA
Mines
Williams Lake
Lac La Hache
100 Mile House
Fraser River
Clinton
Cache Creek
Savona
Ashcroft
Highland Valley
Logan Lake
KAMLOOPS
Salmon Arm
Enderby
Armstrong
Falkland
Shuswap Lake
VERNON
Coldstream
Lumby
Okanagan Lake
Oyama
Winfield
Merritt
KELOWNA
Westbank
Peachland
Summerland
Naramata
PENTICTON
Princeton
Hedley
Okanagan Falls
Keremeos
Oliver
Osoyoos
Midway
Grand Forks
Rossland
Castlegar
Robson
NELSON
TRAIL
Montrose
Fruitvale
Salmo
Creston
Yahk
Arrow Lake
Kootenay Lake
Revelstoke
Columbia River
Columbia Icefields
Lake Louise
Banff
Skookumchuck
Kimberley
Cranbrook
Fernie
Crowsnest
Vancouver
Nanaimo
Victoria
Bellingham
CANADA-U.S.A. BORDER
WASHINGTON
IDAHO
MONTANA

LITHOGRAPHED IN CANADA

red income taxes into its accounting system in the year ended June 30, 1978, and to continue to recognize the unrecorded tax allocation balance which had accumulated in prior years by note to the financial statements.

The substantial increase in income taxes results from the increase in income before taxes and the provision for deferred income taxes.

New Appointments

The Board of Directors, at their meeting on January 26, 1978, appointed Mr. R.G. Brodie, President of Merit Oil Co. Ltd., a Director of the Company.

The Board also made the following appointment of officers; Mr. Geoffrey M.O. Solly, P. Eng., the Company's Chief Engineer, was appointed Vice-President, Operations, and Mr. Clifford I. Kleven, C.A., the Company's Treasurer and Controller, was appointed Vice-President, Treasurer and Controller.

For the Board of Directors

Chairman of the Board

President

Vancouver, B.C.
February 6, 1978

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INLAND
NATURAL GAS CO. LTD.

INTERIM REPORT

DECEMBER 31, 1977

INLAND NATURAL GAS CO

CONSOLIDATED STATEMENT OF INCOME

	Six Months Ended Dec. 31, 1977	Six Months Ended Dec. 31, 1976
REVENUE		
Sale of gas	**$ 32,214,300**	$ 22,947,370
Transportation revenue	**637,771**	148,350
Other operating revenue	**210,000**	261,506
	33,062,071	23,357,226
EXPENSES		
Purchase of gas	**20,362,047**	13,565,594
Operation, maintenance and administrative	**2,723,317**	2,514,913
Property, franchise and other taxes	**1,403,155**	1,184,225
Depreciation	**1,366,498**	1,159,039
Interest and expense on long-term debt	**2,032,977**	2,052,669
Other interest	**455,204**	196,217
Interest charged to construction	**(77,034)**	(7,159)
	28,266,164	20,665,498
Income before income taxes	**4,795,907**	2,691,728
Income taxes		
Current	**1,430,671**	387,407
Deferred	**943,008**	—
	2,373,679	387,407
NET INCOME	**2,422,228**	2,304,321
Dividends declared on preference shares	**700,000**	744,000
	$ 1,722,228	$ 1,560,321
EARNINGS PER COMMON SHARE	**$ 0.61**	$ 0.55
Common shares outstanding on December 31st	**2,822,122**	2,822,122
Total gas sales volume (Mcf)		
- Inland	**20,997,629**	19,481,397
- Subsidiaries	**1,694,230**	1,353,252
	22,691,859	20,834,649

CONS

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Net income for
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Approved on beha

The above statements have been prepared from the books of account a

D. *and wholly-owned subsidiary companies*

ATED STATEMENT OF CHANGES N FINANCIAL POSITION

	Six Months Ended Dec. 31, 1977	Six Months Ended Dec. 31, 1976
NG CAPITAL		
months.	**$ 2,422,228**	$ 2,304,321
es to income		
mortization.	**1,458,698**	1,176,447
xes.	**943,008**	—
	4,823,934	3,480,768
d.	**12,000,000**	—
	16,823,934	3,480,768
ORKING CAPITAL		
y, plant		
. . . .	**3,930,913**	4,662,307
nce and		
. . . .	**1,828,849**	1,872,849
m debt.	**284,500**	444,901
ities.	**322,824**	16,634
. . . .	**137,394**	4,160
	6,504,480	7,000,851
SE)		
ITAL.	**(10,319,454)**	3,520,083
it at June 30.	**12,831,046**	7,373,740
DEFICIT		
. . . .	**$ 2,511,592**	$10,893,823

Board

Director

Director

naudited.

TO OUR SHAREHOLDERS

Earnings

Comparative consolidated statements of income and changes in financial position for the six months ended December 31, 1977, are included in this report. Earnings per common share after providing for dividends on preference shares amounted to 61¢ for the six months under review, compared to 55¢ in the corresponding period last year.

Dividends

On January 26, 1978 your Board of Directors declared quarterly Common Dividend No. 57 in the amount of 20¢ per common share to shareholders of record on February 7, 1978. This dividend is payable on February 15, 1978.

Revenue

Inland's natural gas sales volume was 20,997,629 Mcf for the six months under review compared to 19,481,397 in the comparable period a year ago. There are two fortuitous reasons for the significant increase in the gas sales. Firstly, we finally experienced weather which was considerably colder than normal. The weather for the six months was 19% colder than for the same period last year. This weather pattern resulted in a major increase in residential and commercial sales volumes. Secondly, the Company has sold large volumes of gas by way of the East Kootenay Link to Columbia Natural Gas Limited. So far this year we have sold to Columbia approximately 1,924,000 Mcf compared to 800,000 Mcf in the first six months a year ago. These sales depend entirely on the comparative price of gas available from Inland being more favourable

to Columbia than the price from their regular Alberta suppliers. The price of gas is changing rapidly both in Alberta and British Columbia, and it is difficult to predict with any degree of certainty how long or how much gas we can continue to sell to Columbia.

Transportation revenue has increased substantially this winter. This revenue results from an agreement between the Company and Westcoast Transmission Company Limited, whereby under certain conditions Inland takes delivery of Alberta gas at Yahk, B.C. and transports it into its own distribution system for utilization by Inland customers. This allows Westcoast to reduce deliveries to Inland and increase deliveries to the U.S. border, thus assisting Westcoast in fulfilling the requirements of its export customer. Westcoast pays Inland a transportation fee for this service. While this revenue has been substantial in the period under review, and deliveries under this agreement have continued through January, 1978, Westcoast has been unable to provide the Company with any firm commitments for the continuity of these deliveries.

Expense

The cost of gas purchased during the period increased substantially due in part to the increased throughput, but primarily as a result of the 24¢ per Mcf wholesale price increase which became effective last March and which was flowed through in its entirety to our consumers.

The Provincial Government, on recommendation by the B.C. Energy Commission, has directed that a further increase in the wholesale price of natural gas to distributors in the Province go into effect on March 1, 1978. The B.C. Energy Commission has advised the Company that this wholesale price increase amounting to 21¢ per Mcf can also be flowed through in its entirety to Inland's consumers effective March 1, 1978.

Inland's gas supplier, Westcoast Transmission Company Limited, has recently filed with the National Energy Board an application for a major increase in the rates it charges its domestic customers. The impact on your Company if Westcoast is successful in all aspects of its application, would be to increase our present unit cost of gas by approximately 30¢ per Mcf. The Company's present average cost before implementation of the wholesale price increase outlined above, is approximately 90¢ per Mcf. Inland has served notice of intervention in these proceedings which will be held in three phases. The first phase will commence on February 28, 1978.

Income Taxes

Prior to June 30, 1977 the Company followed the taxes payable (flow-through) basis of accounting for income taxes. Under this method the full amount of benefits arising from the claiming of capital cost and other allowances for tax purposes in excess of the related amounts recorded as expense in the accounts (timing differences), was reflected in the income statement in the year when such benefits were realized; no provision was made in the accounts for the income taxes deferred to future periods.

In its decision dated August 31, 1977, the British Columbia Energy Commission allowed the Company's request to include currently in cost of service the allowance for income taxes on utility income calculated on the tax allocation (normalized) basis. The decision instructed the Company to introduce defer-